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In its 19th year

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Global Strategy and Investment Trends by David Fuller www.fullermoney.com

While most stock market indices will probably trade beneath their all-time highs for years, the variation in performance among sectors and shares will remain enormous.

Reversion to the historic mean by stock market valuations inevitably causes investor disillusion.

The stealth bull market in value stocks continues but this is little consolation for those holding TMT stocks and index tracker funds - People are making money in this stock market but they are in the minority. Fortunately, for some investors, the 1990's bubble did not encompass all sectors of the market. As the crowd chased TMTs, and somewhat more conservatively, big capitalisation growth stocks such as General Electric, many small and mid-cap shares fell below their historic mean in terms of both P/E multiples and yields. In March 2000, what have subsequently proved to be the best buys for at least two years, had been shunned as old economy relics. That divergence between TMTs and basic industries such as building and construction, foods and engineering, prompted this publication's recommendation-accompanying headline, "Will This List of Boring (*37*) Stocks Outperform the NASDAQ at Yearend?" - *FM190 (24/03/00)*. Today, low-multiple, high-yield stocks still have the best performing charts, with few exceptions. As with all fashions, this will end, probably when value stocks have been bid up to levels that no longer represent value. Meanwhile, most of the TMTs and big cap stocks still on optimistic valuations appear destined to become cheaper, judging from their overall downtrends. This is all but inevitable, if we examine past cycles, which show that stocks always revert to their historic mean, up to a decade or more after super-cycle bull markets end. The silver lining to this cloud is that we can anticipate some very attractive valuations further down the reversion road, especially in TMTs and growth stocks.

The Oracle of Omaha - Warren Buffett is wise, rich and funny, and offered this homily recently:

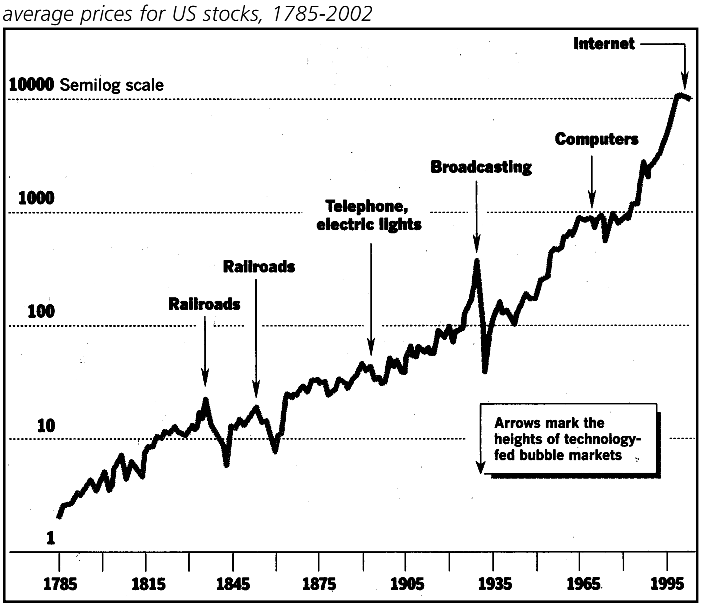
"To refer to a personal taste of mine, I'm going to buy hamburgers for the rest of my life. When hamburgers go down in price, we sing the "Hallelujah Chorus" in the Buffett household. When hamburgers go up, we weep. For most people, it's the same way with everything in life they will be buying - except stocks. When stocks go down and you can get more for your money, people don't like them anymore."

Currently, Warren Buffett is highly critical of many big US companies, particularly regarding management's share options and overly optimistic assumptions for their pension funds. Options are a form of remuneration but most companies do not account for them as an expense. Also, there have been numerous examples of CEOs hyping their share price while exercising their options and selling the stock, causing Buffett to comment that "business leaders view shareholders as patsies, not partners". As for pensions accounting, some of the heightened corporate profitability in the 1990s came from skimming money from overfunded pension plans. Companies projecting the same level of return for these funds in the post-bubble environment are overestimating earnings according to Buffett. Their virtuous circle during the bull market years turns vicious if the pension funds underperform, requiring companies to anti up, which lowers corporate profits.

Spitzer Tackles Merrill Lynch - "Throughout financial history, every great bull market has ended in a frenzy of speculation and a shower of scandals" -. The graph on page 2, "Speculation marches on", produced by Elliott Wave International and reprinted from the International Herald Tribune, shows the DJIA since 1785. It reveals the super-cycle bull market peaks coinciding with technology breakthroughs - railroads, telephones and electric lights, broadcasting, computers and most recently, the internet. Of the earlier speculative binges, I can only remember the super-cycle bull market ending in 1966, coinciding with the commercial use of computers by corporations. Inevitably, there were some scandals associated with booming markets, but nothing like what we have seen in recent years. Consequently there was no 1960s equivalent of Eliot Spitzer, the New York Attorney General, reminiscent of Eliot Ness of Chicago fame during the bootleg era. After subpoenaing thousands of emails, Spitzer is using the formidable, albeit little-known Martin Act - an 80-year old state law, which legal experts say gives him sweeping powers to investigate and prosecute "crooked brokerages, penny stock promoters, scam artists and others who commit fraud". First in Spitzer's sights, but far from alone, is Merrill Lynch, which he described as showing a "shocking betrayal of trust" in recommending stocks to customers that its own analysts were denigrating. Well, this story will run and run, as they say, and it will be a bull market in legal fees.

Speculation Marches On

Market peaks that coincided with technology breakthroughs. Annual average prices for US stocks, 1785-2002



SOURCE: Elliott Wave International; " Triumph of the Optimists: 101 Years of Global Investment Returns"

Significantly, the publicity will add to investor disillusion, with a long-term impact on stock prices. Catching the mood, CNBC presenter Maria Bartiromo recently said to an interviewee, "Why should we believe you? No one believes anyone anymore on Wall Street".

OK, that is certainly an overreaction; it is also looking backwards, and the market is a discounting mechanism. Nevertheless, she was expressing the public's post-Enron anger. Financial scandals are an assault on the public's trust. It will take time to repair the damage. Meanwhile, regulators and investors will demand higher ethical standards. The latter will also be more circumspect and less likely to regard dividends as "an inefficient use of capital".

Interest Rates and Bonds

- **Central banks will proceed cautiously on rate hikes while oil prices remain high.**

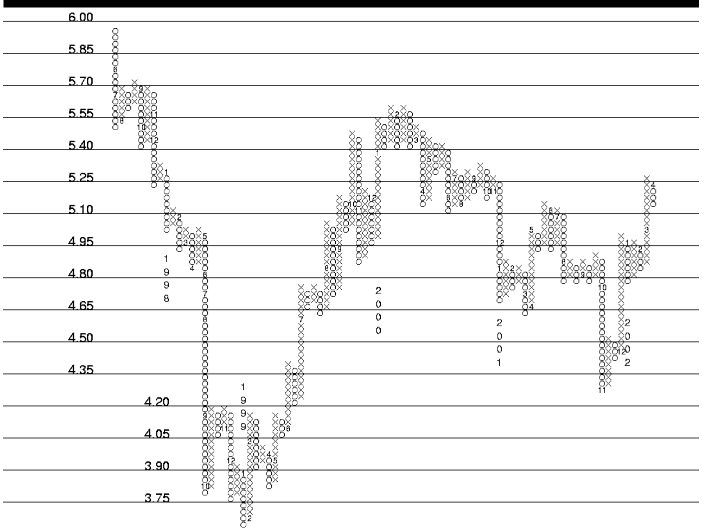
- **The latest surge in Western government long-dated bond yields has been checked but the main trend is still upwards.**

The Bank of Canada is among the latest to raise rates, with a quarter-point increase to 2.25 percent. However the two everyone is watching are the US Federal Reserve and the European Central Bank. Greenspan could easily justify lifting rates from their 40-year low of 1.75 percent, given recent evidence of a recovering economy, albeit patchy, following one of the shallowest recessions in US economic history. However he is concerned about debt levels for consumers and especially corporations, plus the lack of recovery in Euroland and Japan, and most importantly, the recent rise in oil prices on Middle East tensions. The ECB has less reason to hike rates from 3.25 percent, despite inflation above its 2 percent target ceiling, because its projected recovery looks distinctly feeble, especially in Germany. Consequently, central banks will move cautiously in lifting short-term rates, at least until the price of crude oil falls back from its current level of $26.40 (NYME). While rising energy prices are inflationary initially, the medium-term effect is deflationary because it is an OPEC-imposed tax on consumer and corporate spending.

Greenspan's reservations about the pace and/or sustainability of the US economic recovery has temporarily checked the advance in 10-year government bond yields. Consequently the US contract experienced its biggest reaction since January, before encountering some support near the December/January highs. A move to 5.125 would suggest some further correction and a move to 5.425 is required to reaffirm the uptrend since November. Judging from the overall chart, there will be another advance but probably not in the short term. 10-year Euro-bunds have similarly paused and require 5.28 to reaffirm the uptrend. The Australian issue reacted from its December high and lateral trading near 13.3, to test the upper region of support. The overall pattern looks like a V-bottom with right-hand base extension, currently requiring 13.4 to signal additional gains.

US 10 Year Bond Yield (0.025)

Euro-bund 10 Year Bond Yield (0.03)



Strategy for bonds - I'm persisting with my most conservative stance, which is 3-month bills for safety, triple-A corporate bonds for yield and capital appreciation, while avoiding high-yielding issues despite economic recovery prospects. I would also increase cash reserves, because rates will eventually rise and this will be negative for most markets. In futures, having resisted the temptation to jump on somewhat oversold downtrends last month, I have opened a long position in June Eurobunds, looking for a technical rally.

Global Stock Markets

■ **The window of opportunity for many small or mid-cap and high-yielding stocks remains open, at least until the Fed and ECB have raised interest rates two or three times, but most other companies will continue to underperform.**

■ **Corporate profits - from the bad to the misleadingly good.**

■ **The short to medium-term outlook for stock markets remains neutral/positive but for the longer-term, reversion to the historic mean is the dominant theme.**

The small and mid-cap value, high-yielding story is not new. The best opportunity in this category was in March 2000, because the tech mania had driven everything else into the ground. This prompted me to issue my biggest ever list of buy recommendations in FM190 (24/3/00), under the tongue-in-cheek banner, "Will This List of Boring Stocks Outperform the NASDAQ at Yearend?" The drool-inducing yields (although generally ignored at the time) were often higher than the P/E ratios, providing the best value that I have seen since 1987. After the TMT bubble had clearly burst, lots of investment managers became born again value investors, and remain so today. These shares are no longer steals, although many still look OK on a technical and fundamental basis, especially relative to yesterday's stories - those TMTs, often described as "recession-proof" in early 2000. Obviously the TMTs will have some very brisk rallies, initiated by short covering following sell-offs. However, few of these stocks are likely to experience sustained uptrends, let alone retest their 2000 highs in the next few years. Tomorrow's equivalent of TMT, in terms of speculation, will be gold stocks. However I believe the overall preference for small to mid-cap, high-yielding shares will continue, right through the forthcoming cycle of higher short-term interest rates. Monetary tightening will eventually knock these stocks back, but not so much as other companies, and the fashion will re-emerge, refreshed by the shakeout. Portfolio managers will remain value investors, because it sounds respectable in these trying times for the industry, and it makes sense, bubble conditions aside. Why should anyone want to buy high-multiple, low-yielding and now tarnished so-called "growth" shares, for anything other than an occasional oversold rally? Index tracker funds, because they have to, but these are a fashion on the wane.

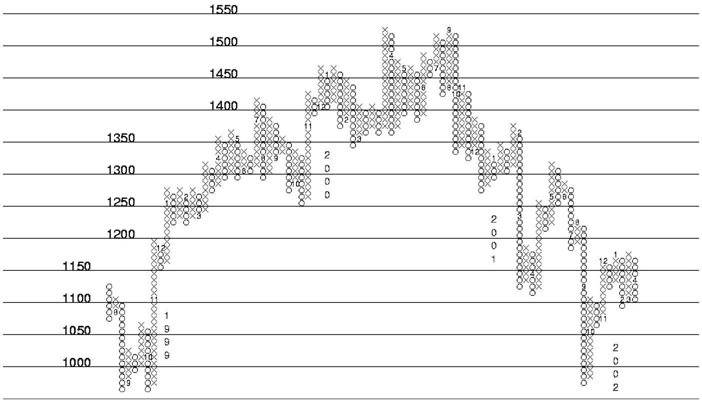
When will interest rates rise in the US and Euroland and how high will they climb? My guess is that the ECB doesn't have a clue, and even The Great One probably hasn't made up his mind yet. They thought they knew, and that it would be soon. Then oil spiked up, necessitating a reassessment because the economic recovery that appeared certain to many only a month ago, could now be in question. Oil subsequently retraced half the rally from its November to January lows but has firmed once again and will obviously remain sensitive to events in the Middle East. Consequently central bankers will be watching petroleum futures and confidence indicators particularly closely, in addition to the usual flow of economic data. My hunch is that only another surge by oil would stay Greenspan's hand beyond the short term. He has to take back at least the 1.75 basis points of rate cuts provided after 9/11, under any other than the most adverse circumstances. The ECB's cheerleading on behalf of the regional economy - by talking growth up and inflation down - is a sign of its anxiety. They are just as likely to get the reverse, which would necessitate a rate hike if the ECB followed its duff mandate. Whatever, I doubt that economic recovery in the US and especially Euroland will look sufficiently durable to justify more than a moderate tightening of monetary policy over the next twelve months.

Reading about the sorry tale of dodgy corporate returns, I'm so glad that I'm not a fundamental analyst! Members of this venerable profession have a daunting job at the best of times, and then they face the plethora of accounting sleights of hand (to put it kindly) from proforma earnings to off balance sheet debt. In truth, turning accountancy tricks probably ranks as mankind's second oldest profession. This black art is often overlooked in bull markets and turned into a sweet science during speculative bubbles. Collective moral indignation only surfaces when share prices are falling. Where do we go from here? Sceptical investment managers now turn to forensic accountants - members of a profession normally specialising in corporate fraud. One positive development is that accounting standards will be tightened, but this is always going to be like drug testing in sports. The cheats are generally a step ahead. As an aside, I wish rating agencies, data providers and broker circulars would feature operating cash flow, as a must watch statistic, right up there with P/E or EBITA ratios and dividend yields. One often hears that cash flow is harder to fudge, although I wouldn't underestimate the creativity of corporate treasurers once fundamental analysts cite it more frequently. Meanwhile, I'll persist with price charts. The trends they reveal range from manic to depressive, but they don't lie. Enron and all other scam shares formed massive top formations long before there was any public talk of misleading information. As for reported "earnings", investors feel they've entered a house of horrors, given all the skeletons falling out of closets in the form of "exceptional write offs" and "extraordinary charges". The consensus expects these to be heavy during the current reporting season, less bad in 2Q and largely out of the way when results for the second half of 2002 are released. My script since late last year is that corporate results for 3Q and 4Q 2002 will be good, due to prior write-offs, cost cutting and a moderate economic recovery. However, the improvement may not be sustainable. A lot depends on petroleum prices and the extent to which central banks raise rates.

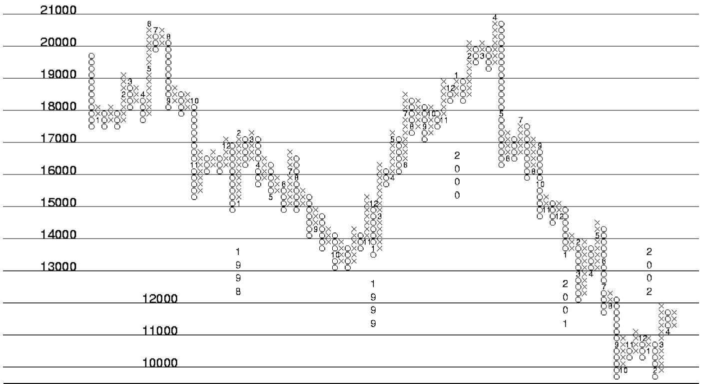
Ranging chart patterns for North American and European Indices still resemble V-bottom with right-hand extension bases. Even Japan's stock market shows technical evidence of recovery, while several of Asia's smaller markets have led the recovery. Even the NASDAQ, which led the way down to last September's lows and has also underperformed this year, recently encountered support near its February low. Consequently the technical picture remains neutral/positive for share indices, provided no sustained breaches of the February troughs occur. However this is a medium-term recovery, not a new bull market. With so many people bearish, why should stock markets move somewhat higher? Markets were inevitably affected recently by events in the Middle East, including higher prices for oil. While the Israeli/Palestinian conflict and conundrum is no closer to being resolved, this situation is no longer deteriorating now that Israel's military is pulling back from occupied regions in the West Bank and some of the Palestinian suicide bombing operations have been rendered temporarily inoperable. Further attempts to broker a peaceful settlement, while unlikely to succeed, should buy a temporary lull in hostilities. Therefore equity markets will focus on other factors, such as earnings reports that are generally less bad than in 4Q 2001 and likely to improve further over the remainder of this year. Also, although a global cycle of somewhat higher short-term interest rates has commenced, hikes in the US and Euroland have been delayed by concern over the Middle East and energy prices. Consequently monetary policy remains stimulative.

With a number of commentators bullish on a longer-term basis, why do you say this is not a new bull market? The main reason is that the latest once-in-a-generation super-cycle bull market ended in 1999/2000. These are always followed by a lengthy reversion to the historic mean, in terms of valuations - *see also FM212 and FM213*. Moreover, history's lesson following speculative excesses is that valuations do not just revert to their mean; they eventually overshoot on the downside, creating outstanding buying opportunities. The unwinding process takes years. When the late-1940s to 1966 super-cycle bull market ended, the subsequent extreme low was not reached until over 8 years later, in end 1974. You won't hear much about reversion to the mean from investment managers - one never does when they are on the wrong side of it, but the process is one of the most logical and predictable long-term cyclical developments in markets. For reference, the mean P/E for the S&P 500 Index is 15, which doesn't sound too far away from today's estimated P/E of 21.8, until we consider the scope for adjustments. Brokerage analysts' estimates of future earnings are notoriously optimistic. Moreover, the quality of those earnings is now being challenged, and we are not only talking about off balance sheet debt and other accountancy sleights of hand. No less a heavyweight than Warren Buffett says management and employee options should be expensed, and that some of America's biggest companies are flattering their earnings with overly optimistic assumptions about the future performance of their employee pension funds. Lastly, the fashion for boosting reported earnings by leveraging balance sheets with debt and using the proceeds for share buybacks is inevitably changing in the post-bubble environment. Corporations are now endeavouring to reduce debt, and secondary offerings will be part of this process, whenever share prices rally sufficiently. Given the post-Enron uncertainty over what earnings actually are, reversion to the mean can be monitored more easily by looking at dividends. The DJIA's yield mean is 4 percent, against 1.76 today. Assuming the market does not collapse, it will take a long time to reach, let alone move temporarily above the dividend mean. Consequently, I maintain that most US and European stock market indices will range beneath their historic highs for years, with bungee-jumping bear markets occurring from the upper boundaries every few years, usually in line with cycles of rising interest rates. As for the NASDAQ, it could take 20 years or more before the 2000 highs are decisively broken, given the extent of its bubble.

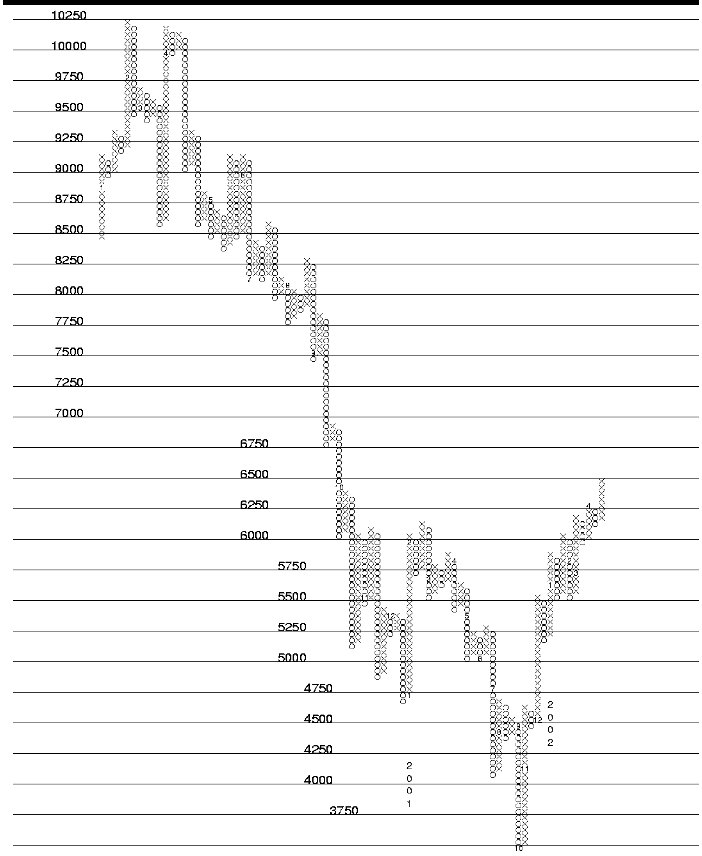
S&P 500 Composite Index (10pt)



Nikkei 225 Stock Average (200pt)



Taiwan Weighted Price Index (50pt)



South Africa JNB Gold Index (25pt)

Chart review of topical and representative stock market indices - *The 3-box reversal point & figure charts shown are based on closing prices and taken from our website. Anyone interested in this chart service, which includes analysis and is updated daily, should register online at www.chartanalysts.com. Price levels mentioned refer to market closes.*

The US's Standard & Poors 500 Composite Index (1104) has been drifting back towards its important February low. If this is broken by a decline to 1080, the V-bottom right-hand extension base characteristics will be further questioned. On daily charts - not shown - a move over 1135 is needed to demonstrate support above the February low and 1180 to suggest some addition recovery into overhead supply. **The NASDAQ Composite Index (1736)** - *not shown* - is pressuring its February low and appears susceptible to a further test of the September/October trough down to 1425. Consequently it requires 1950 to reaffirm support and provide further evidence of base development.

Japan's Nikkei 225 Stock Average (11673) found support at 11000 from the upper side of the September 2001 to March 2002 range. While a break of this level would suggest further easing, a move above 12000 would provide additional evidence of base development.

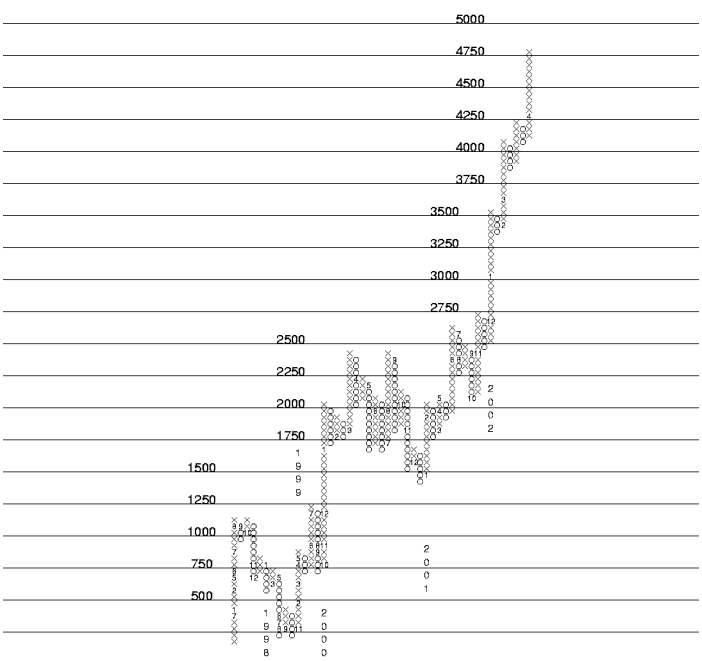
Taiwan's Weighted Price Index (6455) has shown persistent relative strength since its October low and a break in the progression of higher or equal lows is necessary to check pattern consistency.

South Africa's JNB Gold Index (3032) has resumed its advance from the large base and 2625 is needed to check upside momentum beyond a pause.

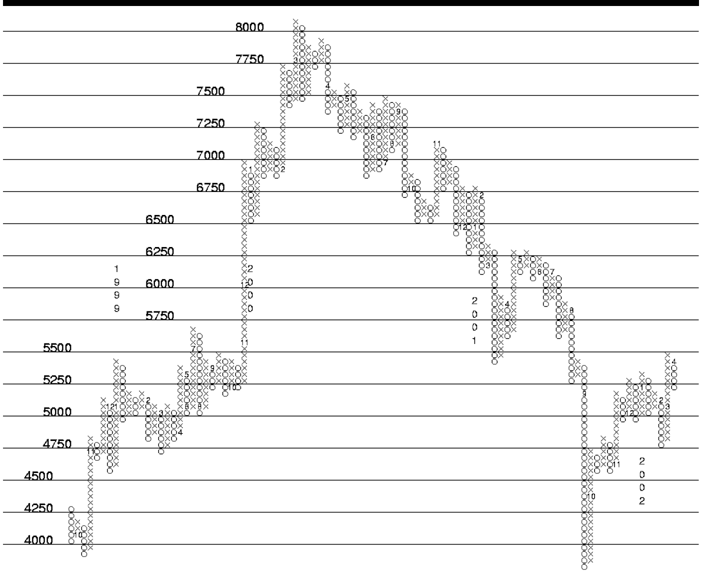
Russia's RSF Index (4750) - *see overleaf* - has been a world-beater since the October reaction low. While this move is becoming overextended, either a greater month-to-month acceleration and/or a decline of more than 5 units of scale (250 points) is required to show trend-ending characteristics.

Germany's DAX Index (5160) - *see overleaf* - has not maintained its push over the January high and needs 5500 to reaffirm the recovery trend. Conversely, a break of the

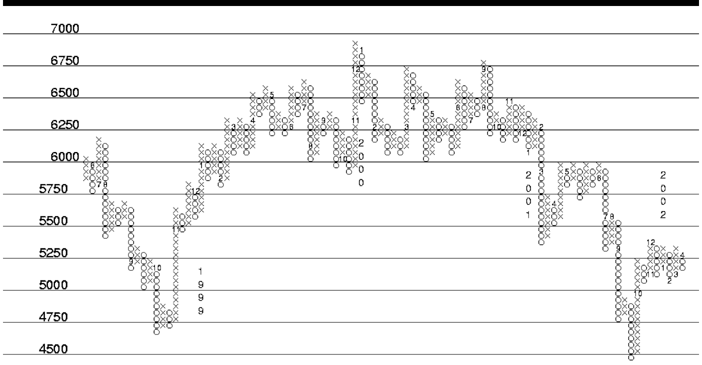
Russian RSF Index (50pt)



German Dax Index (50pt)



United Kingdom FTSE 100 Share Index (50pt)



February low at 4750 would indicate a further retracement of gains.

The UK's FTSE 100 Index (5218) remains rangebound. The important breakout points are 5400 for an additional recovery into heavy overhead supply and a breach of the psychological 5000 level for renewed deterioration.

Strategy for stock markets - The window of opportunity during this medium-term recovery for share markets should remain open for a while longer but investors can already see what will close it. A new cycle of higher short-term interest rates has commenced, albeit gradually, and long-dated government bond yields have risen sharply, JGBs excepted. Consequently, I would select conservatively, continuing to favour high-yield, low-multiple stocks, many of which are medium-sized to smaller companies. I recommended 3 of the more actively traded companies in FM209 (25/10/01) - Boots, Northern Foods and Scottish & Newcastle - all UK firms. The middle of my buying ranges, recommended and reached during the stipulated time period of two months (FM211's release) was, Boots 605p, NFDS 146.125p and SCTN 510p. The median FTSE 100 Index level from 25 October close to its subsequent low over the same period was 5020.75. As of the close on 19th April, the comparative results, not including dividends, were: Boots +16.9%, NFDS +25.2%, SCTN +18.3% and the FTSE +4.4%. The danger period for these and similarly rated shares will be when we are further into the cycle of rising interest rates and/or they trend sufficiently high to no longer qualify as value stocks. Meanwhile, I would deploy breakeven to trailing technical stops. For speculative flavour, I would forget TMTs until there is another accelerated decline, and stay with gold and other mining stocks. Unless you are an expert in this field, the funds are safest. I have significantly reduced my previously biggest position, in the UK listed Merrill Lynch World Mining Trust, an investment trust (closed-end fund) first mentioned in FMP166 (1/02/02) at 110.25p. This subsequently gained over 24% and the trend has neither accelerated relative to its earlier gains, nor has MLWMT's orderly chart pattern shown a loss of trend consistency. However, colleague Tim Parker pointed out that base metal mining shares were rolling over following good rallies, and they constitute a significant proportion of the fund. I'll wait for them to complete this correction before building up my stake in MLWMT again. Meanwhile, I'll probably acquire more gold shares, and recently bought Barrick Gold Corp, quoted in the US. It had underperformed the sector, being out of favour because of its hedging policy, but as the number 2 producer, it won't be ignored for long if the gold price continues to rise. Also, Barrick has recently found more gold in Peru. My view on the Merrill Lynch Gold & General Fund and the Tocqueville Gold Fund, both unit trusts (mutual finds) remains unchanged from FM214. I still hold a small position in the Atlantis Japan Growth Fund but would consider taking profits in the event of another government-engineered surge, looking to repurchase on any setback. I think Japan will be a great recovery story one day, in line with my Triple Play hypothesis, but in the meantime I'll play AJG on a Baby Steps buy-low-sell-high basis, in case there is a lengthy base building phase. In futures, I covered my short positions between 8th and 10th April, and resisted the temptation to go long. I may short again when short-term stochastic indicators suggest another overbought condition.

Currencies

■ **The US dollar is forming an intermediate-term top against other major currencies, the yen excepted.**

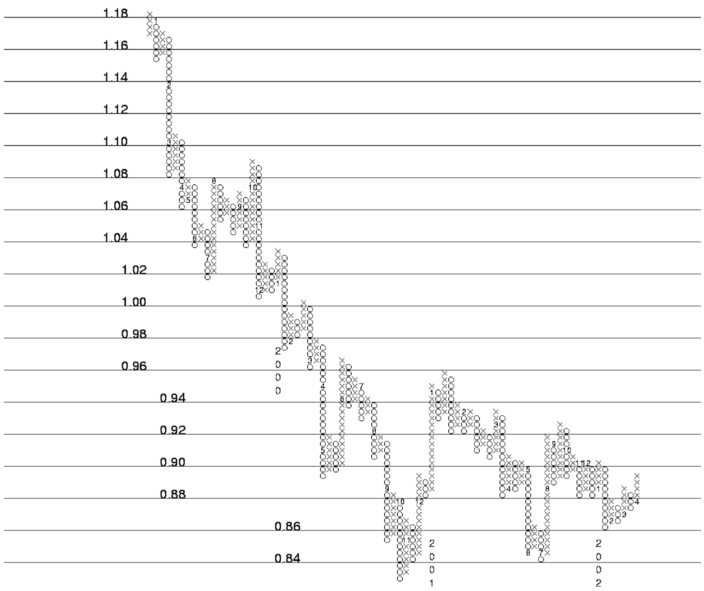
■ **Consensus expectations for additional gains against the yen have declined as currencies range prior to completing their "first step above the base", as taught at TCS.**

Charts have shown for some time that the US dollar was losing upside momentum but traders haven't liked the main alternatives. Let's face it - currency managers have found the euro resistible. They are not impressed by Euroland's past growth or future prospects. They don't like the ECB's deflationary mandate and Wim Duisenberg will be remembered for his haircut, rather than sagacity. Among money managers, the euro package only looks good when compared to the yen, BoJ and Hayami. Add inertia, which causes most people to stay with the trend they know and love until well beyond its sell-by date, and we can see why the dollar has maintained its following. Moreover, everyone knows that the US economy is bouncing back from recession far more quickly than Euroland or Japan. Consequently the greenback may range for a while longer but its Index chart shows an overall loss of momentum, including H & S characteristics. A factor behind this year's slippage from the highs just over 120 is likely to be comparative interest rates. If currencies are ranging quietly, why not take the higher interest rate differential? If the euro is hard to love, why not have the Australian or New Zealand dollars, which provide better yields and would also benefit from a rally in commodity prices. The balance of technical evidence, I suggest, shows that currency traders are gradually moving away from the dollar, except against the yen. At some point, and quite possibly this year, the greenback's gentle and ranging decline will gather pace. Then pundits will find lots of reasons to sell it, including that perennial favourite - the current account deficit. I look for no more than a medium-term correction of a year or two, within the US dollar's very long-term secular recovery, which commenced in 1995. This followed a decline dating from the Bretton Woods Agreement break up in 1971, which was significantly interrupted only during the early 1980s, by the Reagan "Star Wars" military build-up.

People are less bearish of the yen because other currencies have been ranging against it following their January highs. Sentiment has also improved somewhat following evidence of base development for Japan's stock market, talk of tax cuts and Hayami's periodic sterilization of liquidity when the yen approaches its lows. Mad Masaru's term at the BoJ doesn't expire until 20th March 2003 and on past form he will try to prevent the yen from falling until his last breath as Governor. However, judging from the long-term charts, he will have difficulty in preventing a further decline. Meanwhile, the US dollar, euro, sterling, Australian dollar, etc are consolidating in their first step above the base, as taught at The Chart Seminar. It often takes months before these patterns are completed and the current tally stands at 4 and counting. Short-term stochastic indicators show currencies oversold against the yen as I complete this issue, and Japanese finance ministers have already indicated that they do not want to see the dollar below ¥130. A too strong currency and money supply growth of only 3.8 percent (M2+CD) are the main reasons for Japan's deflation. I maintain that its elusive economic recovery will not materialise beyond a blip, let alone become sustainable, without a massive reflation. This means flooding the economy with printed money, not recycling it through the banking system, which only leads to the purchase of more Japanese Government Bonds, as we have long seen. While Hayami probably won't print sufficiently, I suspect someone willing to open the monetary floodgates will replace him in 11 months. Currency markets will anticipate the change. I expect the Australian and New Zealand dollars to lead the next charge against the yen.

US Dollar Index: 117 (Weekly)

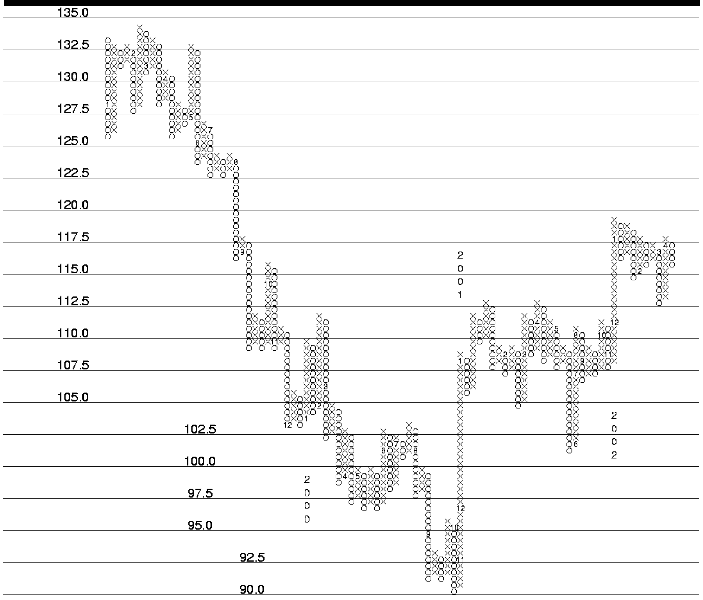
US Dollar per 1 Euro (0.004)



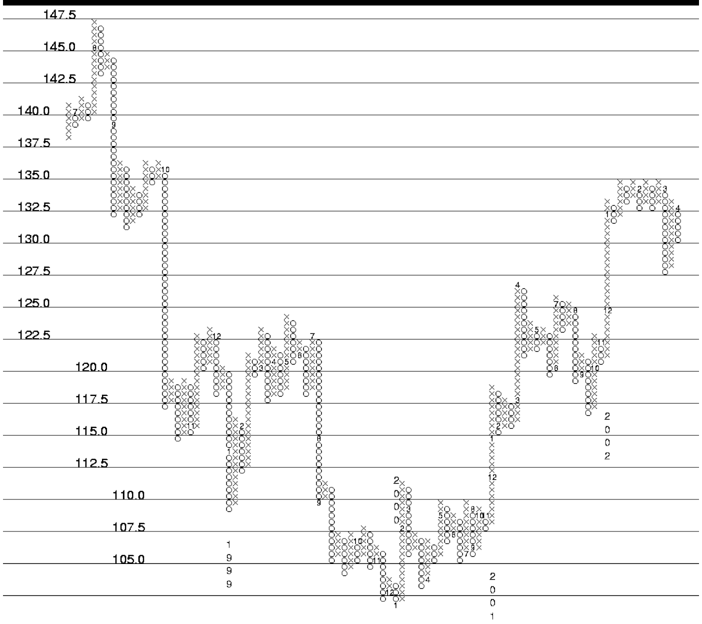
Review of currency and point & figure charts - *These and hundreds of other 3-box reversal closing basis charts are available on our website www.chartanalysts.com and are updated daily. All comments refer to closing levels for US trading hours.*

Euro/dollar ($0.8918) - The gradual recovery since January's low at $0.86 is consistent with the base building hypothesis. The next psychologically significant level is $0.90, representing the highs since last November and it

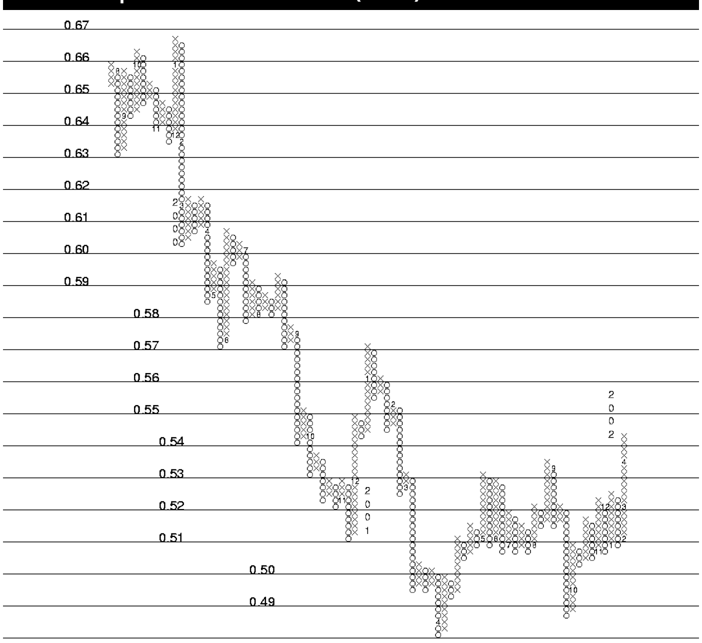
Japanese Yen per 1 Euro (0.5)



Japanese Yen per 1 US Dollar (0.5)



US Dollar per 1 Australian Dollar (0.002)



is also near a downtrend line connecting the January and September 2001 peaks. A break in this year's progression of higher reaction lows, with the latest at $0.872, is required to indicate more than temporary resistance near $0.90.

Euro/yen (¥115.68) - The euro's bounce in March from the upper region of the base was consistent with what I have long described as the first step above the base, within the overall uptrend. A decline to ¥112 is necessary to challenge this hypothesis, which will gain further credibility at ¥118. I expect much higher levels over the medium to longer term.

Dollar/yen (¥129.63) - Resistance from this year's upper boundary turned back the March rebound from above the base. While a decline to ¥127 is required to indicate a test of underlying trading, the size of this overall base, with H&S characteristics dating back to October 1998, suggests that downside risk is limited. Here also, I believe we are looking at the first step above the base. A break above ¥135 should launch a test of the 1998 peak area up to ¥147.

Sterling/yen (¥187.85) - *not shown* - The pound has backed away from the January/February highs near ¥192 but a move to ¥182 is required to indicate test of the base's upper region. The more likely development is an upside breakout, reaffirming the overall uptrend.

Australian dollar/yen (¥70.22) - *not shown* - The Oz dollar remains firm against the yen and ¥67 is required to significantly delay a further recovery in coming weeks.

Australian dollar/US dollar ($0.5417) - The Australian currency has pushed steadily higher since February. While a consolidation is likely before long, a decline beneath $0.53 is now required to suggest an upside failure and further base extension.

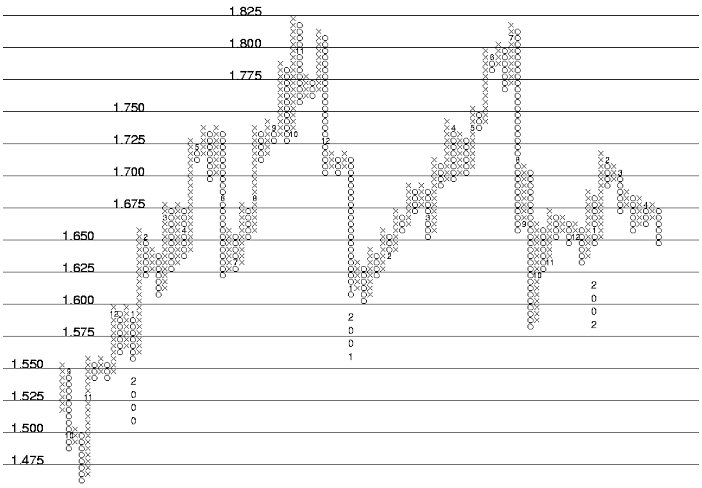
Dollar/Swiss franc (SF1.6440) - This pattern has long looked like an extended top, with the most notable feature following the dollar's October 2000 peak near SF1.82, being a tendency for it to fall faster than it rises. A rally to SF1.68 is now needed to delay a test of the January and September 2001 lows evident between SF1.60 and SF1.58.

Dollar/rand (R10.939) - The rand's collapse last year is shown as an accelerated advance by the dollar to R13.45, with over half the move occurring last December. This is a very dramatic example of the climactic (type 1 of 3) major trend-ending characteristics as taught at The Chart Seminar. A move to R11.30 is now required to suggest a somewhat higher phase of top extension before the dollar retraces a bit more of last year's gains.

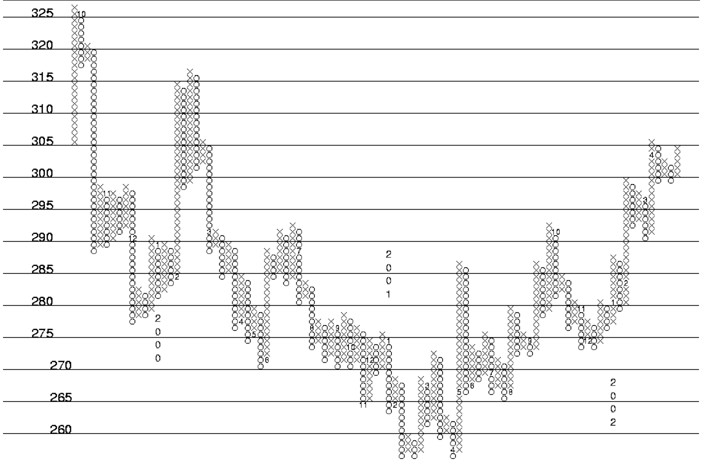
Sterling/dollar ($1.4486) - *not shown* - The pound has encountered support above its band lows dating back to September 2000 and a break in the progression of lower rally highs since last October would suggest a test of the more important resistance commencing at $1.48.

Strategy for currencies - With activity dominated by ranging, opportunities have been limited recently. However

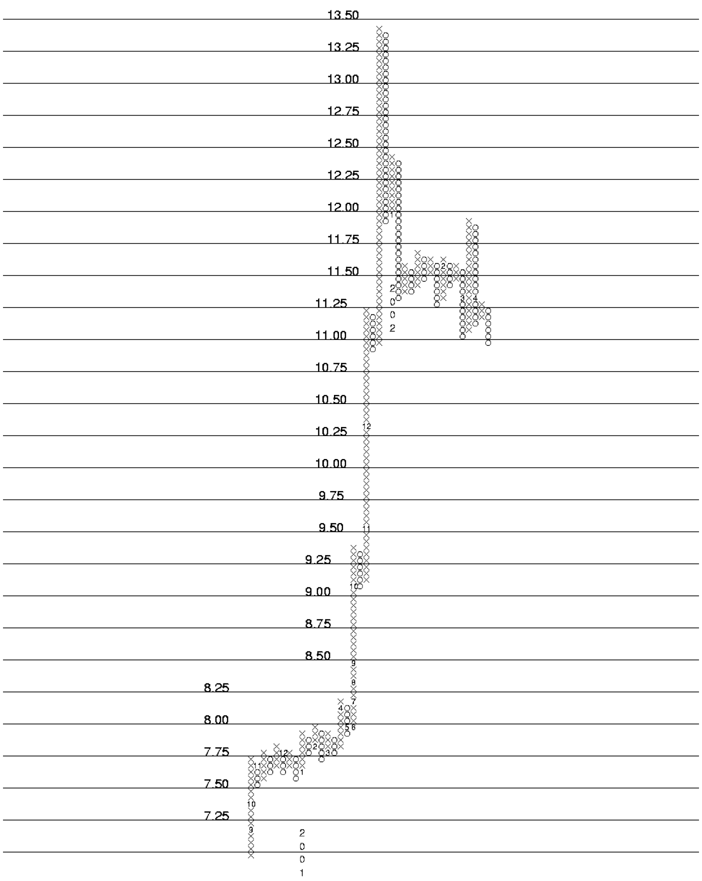
Swiss Franc per 1 US Dollar (0.005)



London Spot Gold (1USD)



South African Rand per 1 US Dollar (0.05)



the euro has been edging higher against the dollar ever since its January low and it is now slightly up on the year to date. I maintain that 2002 will see the single currency break its 3-year downtrend versus the greenback. Consequently, I favour Baby Steps purchases of the euro on easing within its base formation, and I would lighten a bit on the rallies. While I have not been participating myself, the euro is my biggest long position against the yen. Here also, the Baby Steps tactic remains appropriate for harvesting any volatility. However, I expect an eventual upside breakout above ¥120. If this is confirmed by other currencies, I will raise stops on my core position and leverage up - the same strategy used during base completion last December. I also have a somewhat smaller holding in sterling/yen and a bit of dollar/yen, favouring the same tactics as for euro/yen. Better positions during the last two months have been Australian$/yen and New Zealand$/yen, and I suspect Canadian$/yen will be a successful trade but my dealing facility does not allow for these at present. If/when gold takes off, South African rand/yen will be a compelling trade. The rand is a dodgy currency but it shone briefly as the world's strongest when gold romped in 1979/80, and the interest rate differentials are mouth-watering.

Commodities

- **Only the central banks, in tandem with the bullion dealers and hedgers, can push gold back down for a further base extension.**

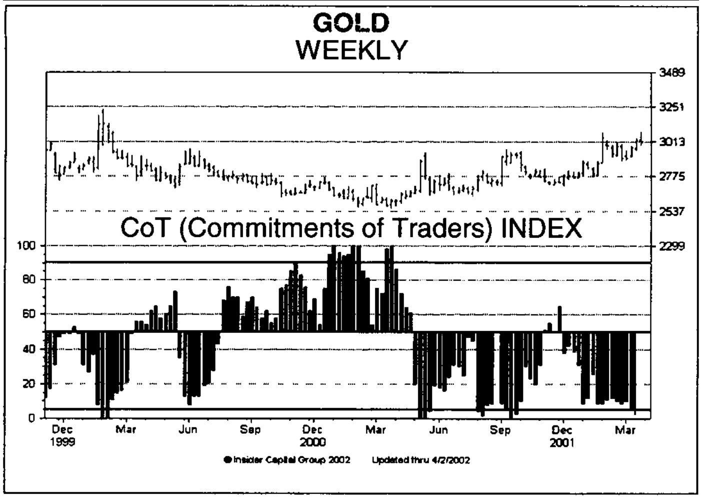
- **Platinum has led the rally in precious metals. Silver and the industrial metals continue to show base development.**

- **Crude oil should encounter further resistance from its top area, despite Middle East tensions.**

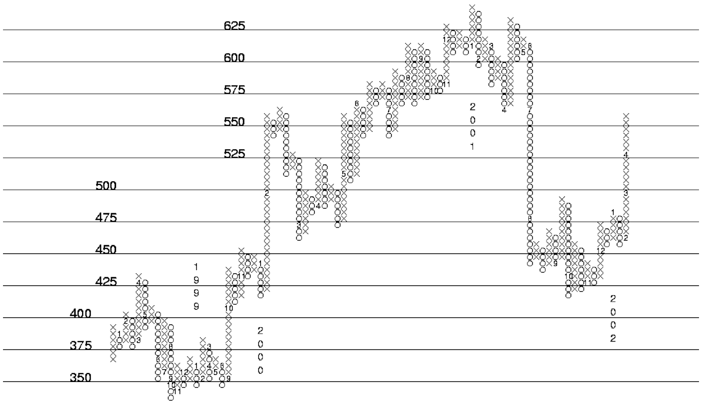
Will central banks cap gold's ranging recovery, either intentionally or inadvertently? They've certainly done it before. For many years the CBs have been happy to lease gold to the bullion-dealing firms at favourable rates, sold it on the futures markets and pursued higher returns in other investments. Meanwhile, most gold mining companies, faced with a static or declining market for their metal, hedged future production with forward sales. These transactions have been massive on occasion, particularly by the bullion dealers, prompting gold bugs to forecast (hope for) the mother of all bear squeezes. It's just possible, when "geniuses" similar to those who ran Long-Term Capital Management, take a good idea that could sensibly be leveraged 10 times and add another nought. However a similar derivatives blow up in the gold market is unlikely, because central banks could supply whatever quantity of bullion was required to prevent a sustained bear squeeze. Nevertheless, Ashanti was bankrupted a few years ago, following an ill-advised hedging policy, so accidents do happen.

In recent months, many mining companies, prompted by gold fund managers and other shareholders, have been

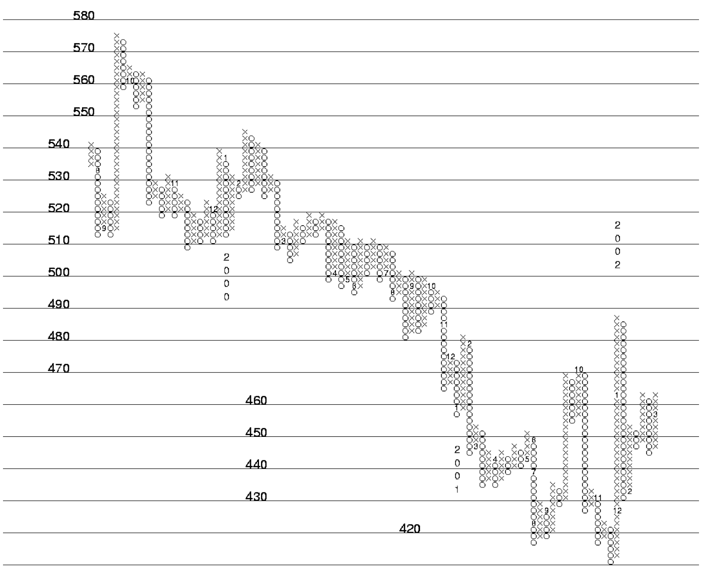
CoT (Commitments of Traders) Index



London Spot Platinum (5USD)

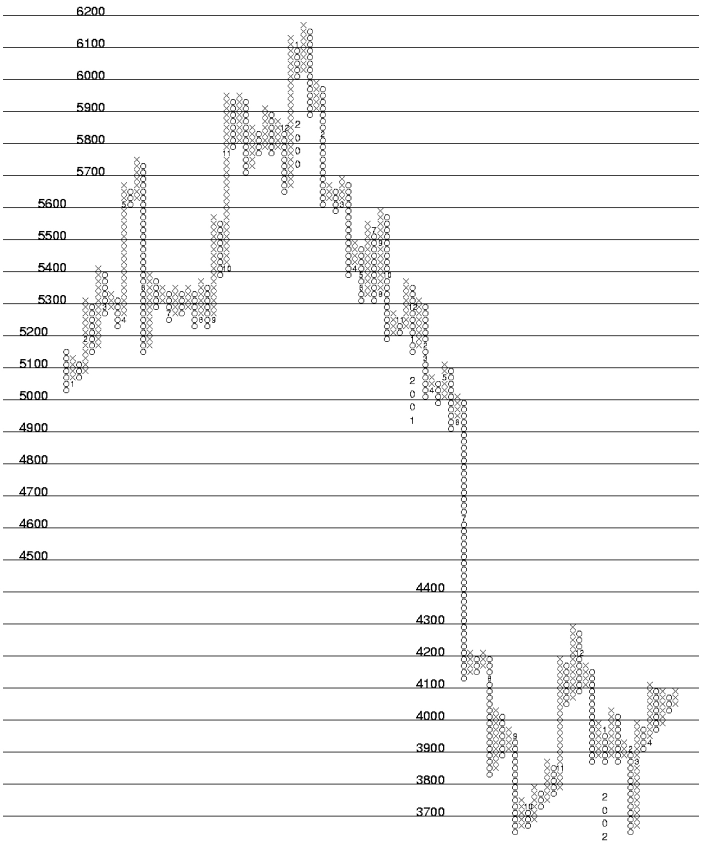


Silver LME 3 Month (2USD)



reducing their forward sales. Is this a smart money indicator as some are claiming? Yes, judging from the price chart, but it depends on what the central banks do, particularly the US Federal Reserve. Their influence is not all-powerful but it certainly hasn't been exhausted in terms of the gold price. Greenspan would not want to see the yellow metal soar but he will also know that the Dow/Gold Ratio remains historically and unsustainably high at 33.5 - see chart in FM214. Central banks have a role to play in the necessary

Tin High Grade LME 3 Month (20USD)



capping of speculative bubbles - they did it with gold in 1980, but it serves no useful purpose to keep the bullion price at a very low level relative to financial assets. I suspect that Greenspan would not be concerned until gold traded at much higher levels. However, European central banks, and notably Gordon Brown's Bank of England, have been doing what most inexperienced investors do - sell near the bottom.

Someone else has also been selling recently, as we can see from the CoT (Commitments of Traders) Index, reproduced from Bullish Review. The lower portion of this graph measures buying and selling by commercial traders, generally regarded as smart money. According to Bullish Review's editor Steve Briese, "…commercials have successfully manipulated gold prices for a number of years. Should prices break out of their defined range *(which he identifies as $270 to $310)*, it would be an indication that commercials have lost control of the market. Though such cases are rare, they often trigger explosive moves" - *see www.BullishReview.com*. Meanwhile, $288 is required to check the ranging uptrend beyond a pause.

Platinum tests its 2000/2001 top area, while silver and tin build bases. Platinum has often been a favourite of precious metal speculators, deterred from buying gold by the leasing/hedging operation. However the price collapsed in mid-2001 when an earlier supply squeeze ended. Nevertheless the backwardation has returned during the current rally, indicating a shortage of refined platinum. It will be interesting to see how it performs now that potential resistance from the underside of the 2000/2001 top is being tested. A rally into this pattern would bode

Crude Oil NYME 2nd Month Continuation (0.2USD)

well for other precious metals. Silver has been a favourite of mine in recent months, because it is a high-beta gold proxy - *see FMP166 (1st February)*. However, this is strictly for trading because of the volatility. I continue to use the Baby Steps buy-low-sell-high tactic, long positions only, given the base characteristics. Tin also shows base characteristics, which is occurring at historic lows. This has understandably led to production cuts and we can expect a major recovery over the longer term. However, unlike gold, tin and other base metals are unlikely to be viewed as safe havens in times of uncertainty, particularly while deflation rather than inflation concerns persist. Without a robust economic rebound, the base building process could be lengthy.

Crude oil's large top formation suggests that any further rallies will be difficult to maintain. The oil price fell sharply following a key day reversal on 4th April - see FMP 172. However it has subsequently pushed back into the lower region of its large top area, partly due to concern over developments in the Middle East. Among petroleum contracts, the absence of contangoes, gas and heating oil excepted, indicates a tightening of supplies. Nevertheless, high prices since 2000 have inevitably led to a significant increase in production capacity, especially from Russia. Therefore any additional forays into the top area, should they occur, are likely to be short-lived.

The Global Economy

■ **The recent rally in oil prices has dampened expectations for economic recovery and energy costs will remain the key variable.**

■ **Concern over the oil price and Middle East tensions will delay and/or slow the rate at which central banks raise rates, as they will be anxious not to snuff out prospects for a moderate economic recovery.**

■ **Gordon Brown's massive tax hike will damage the UK economy.**

Consumer and business sentiment has suffered a mild setback recently. Confidence had rebounded in 4Q 2001 and 1Q 2002, following additional interest rate cuts in response to 9/11, a partial recovery by stock markets, a generally successful war against terrorism and especially lower oil prices. Needless to say, sentiment is a key variable and with the Bush Administration and Federal Reserve providing a "guns and butter" stimulus, expectations for a US-led economic recovery were on the rise. This optimism has been pared back by a surge in oil prices during March and early April, mostly in response to the Israeli/Palestinian crisis and apparent conundrum. It is now widely recognised that a surge in the cost of petroleum represents a massive tax on private consumption and corporate capital expenditure in the oil-importing countries. It was the tripling of oil prices in 1999/2000, more than any other factor, which caused the global recession. Moreover, the Middle East imbroglio fanned concerns not only over the cost of energy, but also the possibility of an escalating military conflict and perhaps even additional terrorist attacks in the West. This mild setback in sentiment has been confirmed recently by lower figures than previously expected for economic data and also confidence indicators. However, on 4th April spot crude oil (NYME) touched $28.35 and then fell back to register a key day reversal - *see FMP172*. This trend-ending signal capped the rally and oil fell back even more quickly than it had risen, despite Iraq's announcement on 8th April that it was suspending oil exports to the West for 30 days. Oil will remain the key variable for the global economy. Around $25 a barrel the influence is broadly neutral, even if the greenback remains generally firm. However every 1-dollar rise above this level would act as an increasing restraint on GDP growth, with this influence pared somewhat if the price of natural gas stays below $5. Should crude become established above $30 for any reason, the global economy would eventually slide back into a recession steeper than seen in 2001. Conversely, every additional 1-dollar decline below $20 would be increasingly stimulative for the world's GDP.

Whatever happens, the economies of Euroland and

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especially Japan will continue to lag behind the US. The Fed moved first and most aggressively in pressing the monetary accelerator last year, taking short-term rates to a 40-year low at 1.75 percent, compared to 3.25 for Euroland and 4 in the UK. Japan's rates were already near zero but with money supply edging up to only 3.8 percent, monetary stimulus remains woefully inadequate. Meanwhile, the US has announced its largest ever increase in military spending, in numerical terms. In contrast, Euroland's "Stability Pact", intended to keep budget deficits below 3 percent, leaves very little scope for a fiscal boost. The UK is increasing fiscal spending but tax hikes will slow consumer spending. Japan has been reducing government spending because of runaway debt. I maintain that the US economy will grow by at least 2 to 3 percent this year. Contributing factors, other than interest rates, the earlier decline by crude oil and fiscal spending, include lower inventories, the stock market recovery since 21st September, generally stable house prices, interest-free financing and price discounts. Consequently business activity has edged higher and consumer spending has experienced only a mild slowdown over the last year.

While a US economic rebound can only be positive for other economies, it will prove to be less of an engine for global growth than generally expected. Without a prior slump in US consumer spending, there will be no surge in demand this year. Moreover, higher interest rates will deter consumers proportionately. America's military spending will help the domestic rather than international economy, with only minor exceptions. Also, the US recovery is likely to be moderate, restrained by corporate debt problems, the absence of a roaring bull market and a less accommodative monetary policy by the Fed in months ahead. Anxious officials in Euroland and Japan are trying to talk up their economies, as we see with the ECB's Arnout Wellink, reported by Bloomberg on 13th April: "The (*recovery*) train is on its way and is accelerating". Staying with this analogy, the US train is pulling away but its coupling to other countries is tenuous, because the latter have not done enough to stimulate GDP growth. Economic recoveries in Europe and Japan over the next year or two will be very moderate. Asia's smaller developed economies will do better, having avoided the worst of Japan's deflationary problems, and because they are more closely allied to the US.

I have been warning that UK Chancellor of the Exchequer Gordon Brown was gradually eroding Britain's competitiveness for years. His massive nearly £8 billion tax hike, via National Insurance on 17th April, is a leap too far, encouraged by people who naively said they would not mind paying higher taxes for better public services, instead of calling for better value from the considerable funds already provided. Will the Government use the additional money it is taking from companies and the public wisely? That would be a first. Meanwhile, a tax-weakened economy is a disservice to all. I agree with economist Roger Nightingale's pithy comment: "Does the Chancellor appreciate the risks he is running? He has seen the British economy outperform those in continental Europe by a full 40% in the last twelve years. Why, in that case, would he now pursue the very policies that are arguably the cause of the latter's failure? Is he conceited enough to suppose that it was he, rather than the country's relatively low taxation, that was responsible for the economy's favourable performance in recent years? Does he think that he, Canute-like, can ward off economics anaemia even while he lifts unaccountable spending on non-productive assets to European levels? Vanitas Vanitatum!"

And Finally…

C2F2 - an exciting new service from Stockcube Research - If you are the least bit interested in currencies, commodities and financial futures, I recommend that you visit www.chartanalysts.com, click on C2F2 and take the tour of this great new service. C2F2 combines all the sophistication of a really good website, with Stockcube's technical research and trading strategies. It replaces our Daily Market Analyses, familiar to many of you, and has far more features. Interesting situations are highlighted daily, and it is also ideal for conducting your own assessment of opportunities.

International Federation of Technical Analysts - Annual Conference - The theme for this year's Conference, held in London on 10th through 12th October 2002, is "Applying Technical Analysis to Enhance Returns". I'll be speaking along with at least 19 other people. The IFTA Conference is quite an event - check it out on www.sta-uk.org/ifta_2002.htm.

The earliest target date for FM216 is Friday 24th May.

> *"The last century proves that market irrationality of an extreme kind periodically erupts - and compellingly suggests that investors wanting to do well had better learn how to deal with the next outbreak."*
>
> Warren Buffett

Best regards - David Fuller

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